

# Economic inefficiencies and over-regulation in air transportation – current issues in Europe

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INAIR 2013 Conference, 7-8 November 2013, Bratislava



Knowledge for Tomorrow



# Overview

1. Introduction
2. Framework: Some fundamental changes in air transport
3. Do all stakeholders work efficiently?
  1. Airlines
  2. Airports
  3. Regulators / Policymakers
4. Conclusion



# 1. Introduction

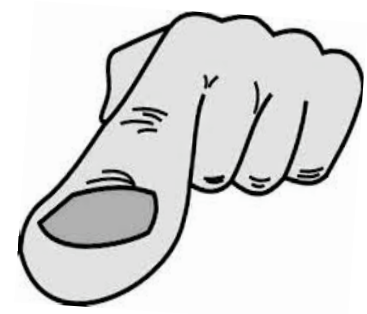
## What is efficiency?

- To do things right!
- Profit-maximization (company resp. total welfare level)

## Is air transport provided in an efficient way?

## Where – in the sector – are efficiency gaps worth pointing a finger at?

- Airline-related issues
- Airport-related issues
- Policy-related issues



## 2. Some fundamental changes in air transport

- The world has changed, new economies have emerged
  - BRIC was only the beginning!
  - Declining dominance of Japan-US-Europe-axis
  - New traffic flows
- **Cost increases** (fuel, security, environmental...)
- **Liberalized vs. isolated** (air transport) markets



## 2. Some fundamental changes in air transport

- **LCC operating in growing P2P markets, taking over the bulk of continental traffic**

➔ **Air travel = commodity**



- **However, airports do not all grow at the same pace**

- **LCC need cost-efficient airports and ATM** to be able to implement their business model



- **Network carriers need sufficient hub capacities** to grow on long haul markets where they are condemned to succeed

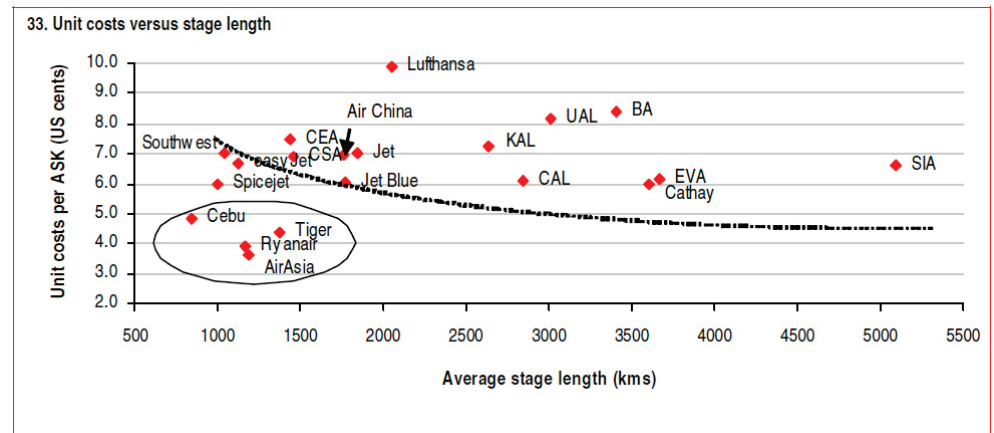




# 3. Do all stakeholders work efficiently?

## 3.1 Airlines

- Low Cost Carriers: efficient business models
  - Low operating costs



www.airlinetrends.com

- Main risk: External cost increases
  - Charges
  - Taxes
  - Fuel
  - Security...



# 3. Do all stakeholders work efficiently?

## 3.1 Airlines

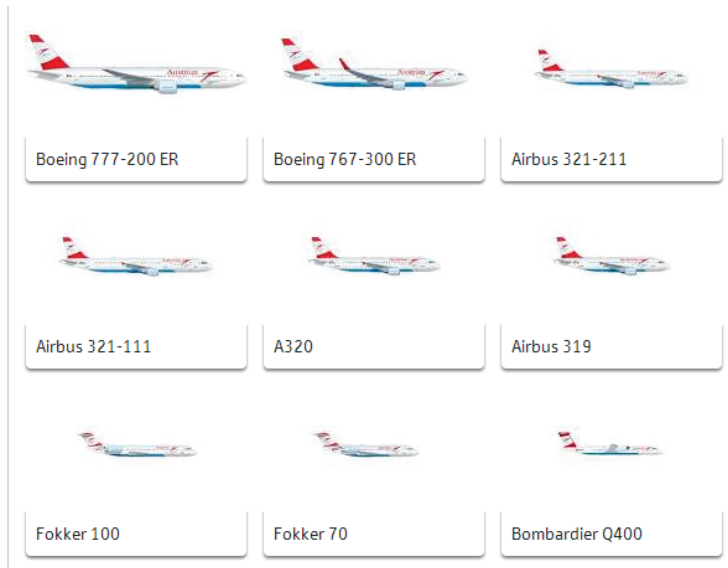
- **Legacy carriers: Sustainable business models?**
  - Small, mixed fleets

### AUA:

76 aircraft

8 aircraft types

4 manufacturers



### Ryanair:

303 aircraft

1 aircraft type

1 manufacturer



# 3. Do all stakeholders work efficiently?

## 3.1 Airlines

- **Legacy carriers: Sustainable business models?**
  - Small, mixed fleets
  - **High overhead costs**
    - General Overhead

### Headquarters LH



Cologne:  
Built 2006  
to be closed 2017  
Cost: ??? €



FRA:  
Cost: > 200 Mio €

### Headquarters Ryanair / easyjet



Ryanair old HQ (left):  
Cost: 3,2 Mio. € +  
244,000 € rent p.a.  
Ryanair new HQ:  
Cost: 20 Mio. € minus  
annual rents from 3rd  
parties



easyJet HQ:  
former aircraft hangar  
Cost: ??? €



# 3. Do all stakeholders work efficiently?

## 3.1 Airlines

- **Legacy carriers: Sustainable business models?**

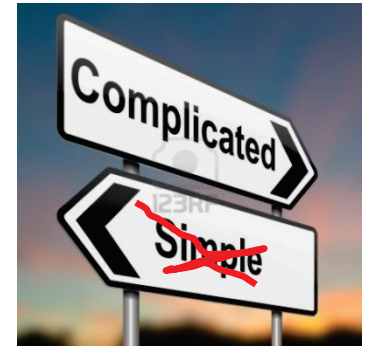
- Small, mixed fleets
- High overhead costs

- **Old-school pricing / Frequent Flyer Programmes:**

Why make things simple when one can make them complicated?

- FRA-JFK oneway 2,627 € (economy), return from 548 €
- Reward ticket DUS-Paris v.v.: 30,000 miles + 144 € Tax
- 30,000 miles = up to 120 return flights in economy class
- Normal ticket same date: 48 € + 50 € Tax = 98 €
- Spiegel.de: „Lufthansa miles have a purchasing power similar to the Sudanese Pound“

<http://www.spiegel.de/wirtschaft/service/lufthansa-schlechterer-service-als-bei-der-bahn-a-925569.html>



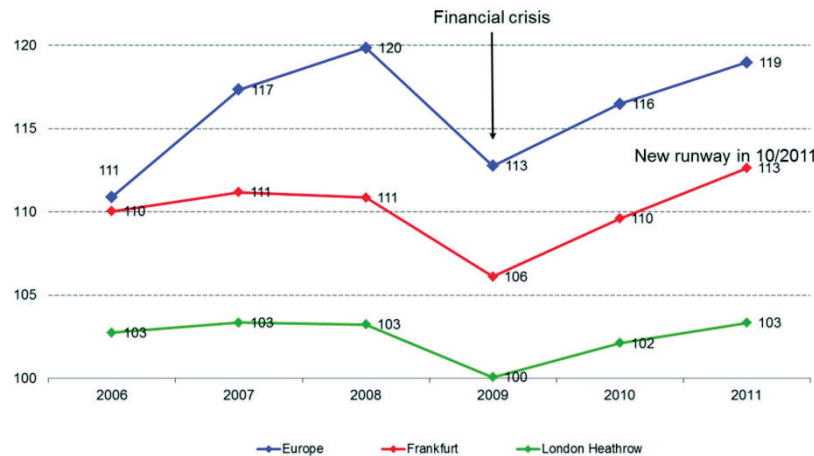
➡ **Sooner or later, passengers will notice they get ripped off**

# 3. Do all stakeholders work efficiently?

## 3.2 Airports

- Is capacity provided where needed?
  - No !
  - **Overcapacity vs. underinvestment**

Aircraft Movements in Europe, Frankfurt and Heathrow



Source: DLR

### Ciudad Real Airport, Spain

Spain's €1bn white elephant airport could be yours for just €100m

The first private international airport in Spain that turned into one of the country's biggest white elephants is being sold off for just €100m.



Ten million passengers a year were expected to pass through its 28,000 sq ft terminal. But it opened during one of the worst recessions ever seen, with Spain particularly hard-hit. Photo: Alamy



By Andrew Trotman

4:20PM BST 07 Aug 2013

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The airport at Ciudad Real in La Mancha cost €1.1bn to build but was closed in April 2012 after just four years in operation when its management company fell into receivership.

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Source: <http://www.telegraph.co.uk/finance/newsbysector/transport/10228961/Spains-1bn-white-elephant-airport-could-be-yours-for-just-100m.html>

# 3. Do all stakeholders work efficiently?

## 3.2 Airports

- **Overpriced investments**

- Berlin (too small and too expensive)
- Dublin Terminal 2 ( „gold-plated“ €609M terminal)
- ...



- Airline views hardly considered in planning processes

- Cost
- Night curfews...

- „Formula“ applied at many regional airports:  
Expensive infrastructure  
+ Public Service Obligations (as low charges are objected by EU)  
= high costs and low traffic



# 3. Do all stakeholders work efficiently?

## 3.3 Regulators / Policymakers

- **Slot Allocation:**
  - Grandfathering at highly constrained airports, even for small aircraft (=low slot productivity)
  - Market entry for LCC at hubs difficult
- **Bilateral Air Service Agreements:** Cap on frequencies/destinations to protect national carriers
- **Consumer protection:**
  - 250-600 EUR compensation in case of cancelled flights, regardless of the ticket price
  - Railways: 25% of ticket price



# 3. Do all stakeholders work efficiently?

## 3.3 Regulators / Policymakers

- **Airline Mergers:**
  - Trans-border mergers virtually impossible due to ownership clauses
  - This promotes the high level of fragmentation in the industry
- **Taxation:**
  - High passenger duties especially in Europe
  - Incentive to operate smaller, less fuel-efficient aircraft and to charge higher fares
  - Negative welfare effect as air transport facilitates global trade
- **ATM / Single European Sky:** No progress



**Rising costs, rising fares, declining demand!**

**Is there any industrie which is less regulated than air travel?**



## 4. Necessary steps

### **Traditional airlines:**

- Simplify your business to reduce costs!
  - You don't need 8 different aircraft types and a €200M HQ to produce a good inflight product!
  - Is it really essential for your platinum customer to select between Porsche Cayenne and Mercedes for the aircraft transfer?
- Provide your consumer with a real added value, and not with fakes!
- ...

### **Airports:**

- Earn your money with retailing, parking etc.!
- Keep your costs down and your processes simple, avoid gold-plating!
- Do not invest in infrastructures that are not needed by the airlines!
- ...

### **Policymakers: Treat air transport like other industries!**

- Let the suppliers decide where to invest!
- Market protection reduces consumer welfare ... and promotes inefficiencies with the carriers!
- Don't charge taxes exceeding the ticket price!
- Does overexaggerated consumer protection really help the customer?
- ...

# Thank you!

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